

Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended and P.A. 71 of 1919, as amended.

Local Unit of Government Type <input type="checkbox"/> County <input type="checkbox"/> City <input type="checkbox"/> Twp <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Unit Name South County Sewer & Water Authority	County Kalamazoo
Fiscal Year End 3-31-06	Opinion Date 7-14-06	Date Audit Report Submitted to State 9-28-06	

We affirm that:

We are certified public accountants licensed to practice in Michigan.

We further affirm the following material, "no" responses have been disclosed in the financial statements, including the notes, or in the Management Letter (report of comments and recommendations).

YES ☒ NO ☐ Check each applicable box below. (See instructions for further detail.)

1. ☒ ☐ All required component units/funds/agencies of the local unit are included in the financial statements and/or disclosed in the reporting entity notes to the financial statements as necessary.
2. ☒ ☐ There are no accumulated deficits in one or more of this unit's unreserved fund balances/unrestricted net assets (P.A. 275 of 1980) or the local unit has not exceeded its budget for expenditures.
3. ☒ ☐ The local unit is in compliance with the Uniform Chart of Accounts issued by the Department of Treasury.
4. ☒ ☐ The local unit has adopted a budget for all required funds.
5. ☒ ☐ A public hearing on the budget was held in accordance with State statute.
6. ☒ ☐ The local unit has not violated the Municipal Finance Act, an order issued under the Emergency Municipal Loan Act, or other guidance as issued by the Local Audit and Finance Division.
7. ☒ ☐ The local unit has not been delinquent in distributing tax revenues that were collected for another taxing unit.
8. ☒ ☐ The local unit only holds deposits/investments that comply with statutory requirements.
9. ☒ ☐ The local unit has no illegal or unauthorized expenditures that came to our attention as defined in the *Bulletin for Audits of Local Units of Government in Michigan*, as revised (see Appendix H of Bulletin).
10. ☒ ☐ There are no indications of defalcation, fraud or embezzlement, which came to our attention during the course of our audit that have not been previously communicated to the Local Audit and Finance Division (LAFD). If there is such activity that has not been communicated, please submit a separate report under separate cover.
11. ☐ ☒ The local unit is free of repeated comments from previous years.
12. ☒ ☐ The audit opinion is UNQUALIFIED.
13. ☒ ☐ The local unit has complied with GASB 34 or GASB 34 as modified by MCGAA Statement #7 and other generally accepted accounting principles (GAAP).
14. ☒ ☐ The board or council approves all invoices prior to payment as required by charter or statute.
15. ☒ ☐ To our knowledge, bank reconciliations that were reviewed were performed timely.

If a local unit of government (authorities and commissions included) is operating within the boundaries of the audited entity and is not included in this or any other audit report, nor do they obtain a stand-alone audit, please enclose the name(s), address(es), and a description(s) of the authority and/or commission.

I, the undersigned, certify that this statement is complete and accurate in all respects.

We have enclosed the following:	Enclosed	Not Required (enter a brief justification)	
Financial Statements	<input checked="" type="checkbox"/>		
The letter of Comments and Recommendations	<input checked="" type="checkbox"/>		
Other (Describe)	<input checked="" type="checkbox"/>	Report to the Board following SAS#61 guidance.	
Certified Public Accountant (Firm Name) Seber Tans, PLC		Telephone Number 269-343-8180	
Street Address 555 W. Crosstown Parkway, Suite 304		City Kalamazoo	State MI
Zip 49008			
Authorizing CPA Signature <i>Matthew A Howard, CPA</i>		Printed Name Mathew Howard	License Number 1101013253

SOUTH COUNTY SEWER AND WATER AUTHORITY
FINANCIAL STATEMENTS AND SUPPLEMENTAL INFORMATION

For the Years Ended March 31, 2006 and 2005

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SEBER TANS, PLC

CONSULTANTS & CERTIFIED PUBLIC ACCOUNTANTS
INDEPENDENT AUDITORS' REPORT

To the Board of Commissioners
South County Sewer and Water Authority

We have audited the accompanying financial statements of South County Sewer and Water Authority as of and for the years ended March 31, 2006 and 2005 as listed in the table of contents. These financial statements are the responsibility of the South County Sewer and Water Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion the financial statements referred to above present fairly, in all material respects, the financial position of South County Sewer and Water Authority at March 31, 2006 and 2005, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Management's discussion and analysis (identified in the table of contents) is not a required part of the basic financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America. We applied certain limited procedures consisting principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. We did not audit the information and express no opinion on it.

Our audits were performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying financial information listed as supplemental information in the table of contents is presented for the purpose of additional analysis and is not a required part of the basic financial statements of the South County Sewer and Water Authority. The supplemental information has been subjected to the auditing procedures applied in the audits of financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

Seber Tans, PLC
Seber Tans, PLC
Kalamazoo, Michigan

July 14, 2006

SOUTH COUNTY SEWER AND WATER AUTHORITY MANAGEMENT'S DISCUSSION AND ANALYSIS

Using This Annual Report

This annual report consists of the Statements of Net Assets, the Statements of Revenues, Expenses and Changes in Net Assets, and the Statements of Cash Flows. Along with the footnotes, they provide detailed financial information concerning the Authority. This section, Management's Discussion and Analysis, is intended to provide an overview of the Authority's financial condition, results of operations, and other key information.

Financial Overview

In analyzing the Authority's financial position, it is important to recognize the mission of the Authority. From a financial perspective, the Authority's core objective is to manage the long-term costs of providing sanitary sewer service to the businesses and residents (collectively the Users) of participating Municipalities. The Authority acts as an agent of the participating Municipalities. The quarterly amounts charged to Users approximate the operating costs incurred by the Authority in providing sanitary sewer service. In addition to the long-term operating costs of providing sanitary sewer service, the Authority is responsible for the repayment of bonds and other debt obligations incurred to finance the construction of the sanitary sewer system and used to purchase long-term sewer capacity. Charges for capital costs are generally made to the benefiting party, the land owner and/or developer, at the time the infrastructure is constructed.

A significant non-cash expense of the Authority is depreciation. Depreciation expense represents costs associated with the construction of the sanitary sewer system that are financed by long-term debt obligations and assessments on the Users' properties. Principal payments from assessments and principal payments on long-term financing are not reflected as revenues or expenses of the Authority. For budgeting purposes and for setting user rates, management does not consider depreciation expense.

	2006	2005
Total operating expenses	\$ 359,200	\$ 340,230
Less depreciation and amortization	(186,595)	(184,369)
Operating expenses, net of depreciation and amortization	172,605	155,861
Users	570	549
Annual cost per User	\$ 303	\$ 284
Monthly cost per User	\$ 25	\$ 24

The Authority's costs of operating are primarily affected by treatment charges from the City of Kalamazoo and the costs of services, both contracted and employed personnel. The sanitary sewer system covers a geographic area of approximately 5 square miles, including 15 miles of pipeline. It is envisioned that approximately 50 new users will connect to the sewer system over the next ten years. As new users connect to the sanitary sewer system, it is anticipated that the cost per user will decrease.

The Authority's net assets increased approximately \$326,000 in 2006 and \$12,000 in 2005. Net assets increased in 2006 and 2005 primarily as a result of contributed capital from special assessments and connection fee contracts. The authority recognized contributed capital of \$415,800 and \$82,000 as two special assessment districts and 9 new users were added to the sanitary sewer system.

**SOUTH COUNTY SEWER AND WATER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS**

	<u>2006</u>	<u>2005</u>	<u>% Change</u>
Capital assets	\$ 6,863,209	\$ 6,464,470	6.2
Other assets	<u>4,090,933</u>	<u>4,187,697</u>	-2.3
Total assets	10,954,142	10,652,167	2.8
Long-term liabilities	4,450,318	4,470,520	-0.5
Other liabilities	<u>452,311</u>	<u>456,429</u>	-0.9
Total liabilities	4,902,649	4,926,949	-0.5
Net assets:			
Invested in capital assets net of related debt	2,012,930	1,597,432	26.0
Restricted assets	4,009,484	4,115,967	-2.6
Unrestricted assets	<u>29,079</u>	<u>11,819</u>	---
Total net assets	<u>\$ 6,051,493</u>	<u>\$ 5,725,218</u>	5.7

Restricted net assets represent the total of all assets restricted for the repayment of bond obligations and for future capital improvements. Debt obligations payable exceeded the total restricted net assets of the Authority by approximately \$780,000 and \$790,000 at March 31, 2006 and 2005. This shortfall in assets available to repay the debt results from a number of factors: (1) The Users were originally assessed 80% of the estimated construction cost for the sanitary sewer. (2) As is typical, users were charged a lower initial cost per user in anticipation of normal future growth over time. (3) One User comprising 26% of the total assessment was granted a reduction of \$468,030 from the amount the User was originally assessed. (4) The growth rate anticipated at the time of construction was 10 new units (homes) per year; the growth rate the system has experienced has been 7 new units per year. Over time it is anticipated that the expected average growth rate will be met.

The Authority's ability to manage the repayment of bond debt at a reasonable cost to the Users is a key objective of Management. Management semi-annually reviews the growth rate and estimates future cash flows, and to the extent necessary, Management has implemented a debt service charge for each User on the system. Management annually recommends adjustments to the debt service charge based on a number of factors such as the number of new connection fees, interest rates earned on investments, and the rate at which assessment and connection fee contracts are prepaid. The ultimate cost to the Users will depend chiefly on these three factors.

**SOUTH COUNTY SEWER AND WATER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS**

	<u>2006</u>	<u>2005</u>	<u>% Change</u>
Operating revenue	\$ 183,594	\$ 164,371	11.7
Operating costs	<u>359,200</u>	<u>340,230</u>	5.6
Net loss from operations	(175,606)	(175,859)	0.1
Net non-operating revenue (expenses)	<u>4,081</u>	<u>(51,366)</u>	107.9
Net loss	<u>\$ (171,525)</u>	<u>\$ (227,225)</u>	24.5

Operating revenues increased by 11.7% from 2005 to 2006. This increase resulted from increases in the number of users and from special one time billings for treatment charge adjustments. The increase in operating costs from operations resulted primarily from an increase in treatment charges from the City of Kalamazoo's regional treatment facility. The increase in net non-operating revenues resulted primarily from an increase in interest rates paid on the Authority's cash and restricted assets and from administrative fees charged for administering the Sprinkle Road project. The Authority continued to have a significant negative net interest margin. The negative interest margin amounted to \$31,994 and \$56,289 for 2006 and 2005, respectively. The negative interest margin resulted primarily from two factors: 1) low interest rates and 2) an excess of debt payable over assessments receivable and investments. The low interest rates that have prevailed in the general market for the last few years have resulted in a number of Users accelerating their payments on assessments. Management reviews the cost effectiveness of redeeming or refunding bonds on an annual basis.

As described earlier, the bonds payable exceeded interest bearing assets restricted for payment of bonds by approximately \$780,000 and \$790,000 at March 31, 2006 and 2005, respectively. Also as described previously, the primary sources available to the Authority to reduce this negative margin are connection fees from User growth (new customers) and from debt service fees charged to all Users. The Authority Board closely monitors the debt requirements and each year makes recommendations to the participating municipalities for adjustments to the debt service fee as needed to maintain long-term surplus cash flow for debt repayment. The participating municipalities have, to date, increased debt service fees according to the recommendations.

Capital Asset and Debt Administration

In fiscal 2006, the Authority partnered with Pavilion Township and implemented a sanitary sewer project along Sprinkle Road in Pavilion Township. The project cost approximately \$599,000 and was financed by a combination of assessments, utilization of restricted cash, and borrowings.

Restricted funds on hand	\$ 170,000
Long-term borrowings from Pavilion Township Sewer Fund	213,000
Long-term borrowings under Township of Pavillion Act 99 Installment Purchase Agreement	<u>216,000</u>
	<u>\$ 599,000</u>

SOUTH COUNTY SEWER AND WATER AUTHORITY MANAGEMENT'S DISCUSSION AND ANALYSIS

The Authority incurred only minimal costs for repairs to the sanitary sewer in both 2006 and 2005. In fiscal 2007 it is not anticipated the Authority will incur significant debt for repairs and/or replacements, as the sewer system was newly constructed in 1998.

Economic Factors and Next Year's Rates

Each year, the Authority monitors its cash flow for operating expenses and makes recommendations to the participating municipalities for rate increases necessary to fund operations and maintenance. It is anticipated that User growth and cost efficiency measures by Management will minimize the effect of future operating cost increases over the upcoming year.

Contacting the Authority's Management

This financial report is intended to provide our citizens, taxpayers, customers, and investors with a general overview of the accountability for the money it receives. If you have questions about this report or need additional information, we welcome you to contact Rich Pierson, Director, or Cindy Chapman, Assistant Director, South County Sewer & Water Authority, at 269-321-8925.

SOUTH COUNTY SEWER AND WATER AUTHORITY
STATEMENTS OF NET ASSETS
March 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 47,577	\$ 30,181
Contracts receivable from municipalities, no allowance for doubtful accounts	222,000	200,000
Other contracts receivable, no allowance for doubtful accounts	<u>25,000</u>	<u>20,000</u>
TOTAL CURRENT ASSETS	294,577	250,181
OTHER ASSETS		
Contracts receivable, excluding current portion	2,137,328	1,995,373
Other contracts receivable, excluding current portion	166,984	160,447
Start-up costs, net of amortization	---	5,177
Bond issue discount, net of amortization	33,872	36,372
Restricted cash and investments	<u>1,458,172</u>	<u>1,740,147</u>
TOTAL OTHER ASSETS	3,796,356	3,937,516
PROPERTY AND EQUIPMENT		
Fixed assets, net of accumulated depreciation of \$998,331 and \$814,235	<u>6,863,209</u>	<u>6,464,470</u>
TOTAL ASSETS	<u>\$ 10,954,142</u>	<u>\$ 10,652,167</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	\$ 18,498	\$ 23,539
Accrued interest	62,833	82,890
Current portion of contract debt payable	<u>371,000</u>	<u>350,000</u>
TOTAL CURRENT LIABILITIES	452,331	456,429
LONG-TERM LIABILITIES		
Contract debt payable, less current portion	<u>4,450,318</u>	<u>4,470,520</u>
TOTAL LIABILITIES	4,902,649	4,926,949
NET ASSETS		
Invested in capital assets, net of related debt	2,012,930	1,597,432
Restricted for debt service and other purposes	4,009,484	4,115,967
Unrestricted assets	<u>29,079</u>	<u>11,819</u>
TOTAL NET ASSETS	<u>6,051,493</u>	<u>5,725,218</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 10,954,142</u>	<u>\$ 10,652,167</u>

See Accompanying Notes to the Financial Statements

SOUTH COUNTY SEWER AND WATER AUTHORITY
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN NET ASSETS
For the Years Ended March 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
REVENUES		
Charges for services	\$ 183,594	\$ 164,371
OPERATING EXPENSES		
Salaries and wages	50,605	49,166
Fringe benefits	10,044	9,859
Contracted services	91,332	77,555
Utilities	9,819	11,554
Supplies	3,732	3,201
Maintenance and repairs	7,073	4,526
Depreciation and amortization	186,595	184,369
TOTAL OPERATING EXPENSES	<u>359,200</u>	<u>340,230</u>
OPERATING LOSS	(175,606)	(175,859)
NON-OPERATING REVENUES		
Debt service fees	29,752	20,455
Administrative fee	11,500	---
Interest income on investments	36,164	13,314
Interest income on special assessments	116,259	135,730
Interest income on connection fee contracts	14,563	8,190
TOTAL NON-OPERATING REVENUES	<u>208,238</u>	<u>177,689</u>
NON-OPERATING EXPENSES		
Interest expense	(198,980)	(213,523)
Amortization	(5,177)	(15,532)
TOTAL NON-OPERATING EXPENSES	<u>(204,157)</u>	<u>(229,055)</u>
LOSS BEFORE CONTRIBUTIONS	(171,525)	(227,225)
Capital contributed	497,800	239,243
CHANGE IN NET ASSETS	326,275	12,018
Net assets at beginning of year	5,725,218	5,713,200
NET ASSETS AT END OF YEAR	<u>\$ 6,051,493</u>	<u>\$ 5,725,218</u>

See Accompanying Notes to the Financial Statements

SOUTH COUNTY SEWER AND WATER AUTHORITY
STATEMENTS OF CASH FLOWS
For the Years Ended March 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from users	\$ 183,594	\$ 164,371
Cash payments to suppliers for goods and services	(116,997)	(92,139)
Cash payments to employees for services	(60,649)	(59,026)
NET CASH PROVIDED BY OPERATING ACTIVITIES	5,948	13,206
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Other non-operating revenues	41,252	20,455
Proceeds from connection fees	70,463	84,533
Proceeds from contracts with municipalities	251,845	267,239
Proceeds from contract debt issued	428,518	---
Principal paid on contract debt	(427,720)	(325,000)
Interest paid on contract debt	(219,037)	(210,199)
Acquisition and construction of capital assets	(582,834)	(11,624)
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	(437,513)	(174,596)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest earned on investments and receivables	166,986	157,234
Net proceeds from (investments in) government obligations with maturities greater than 90 days or restricted for capital improvements or debt reduction	281,975	(92,537)
NET CASH PROVIDED BY INVESTING ACTIVITIES	448,961	64,697
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	17,396	(96,693)
 Cash and cash equivalents at beginning of year	 30,181	 126,874
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 47,577</u>	<u>\$ 30,181</u>

See Accompanying Notes to the Financial Statements

	<u>2006</u>	<u>2005</u>
SUPPLEMENTAL DISCLOSURES		
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	\$ (175,606)	\$ (175,859)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation and amortization	186,595	184,369
Increase (decrease) in:		
Accounts payable	<u>(5,041)</u>	<u>4,696</u>
TOTAL CHANGES IN ASSETS AND LIABILITIES INCLUDED IN OPERATING RESULTS	<u>181,554</u>	<u>189,065</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 5,948</u>	<u>\$ 13,206</u>

SOUTH COUNTY SEWER AND WATER AUTHORITY
NOTES TO FINANCIAL STATEMENTS
For the Years Ended March 31, 2006 and 2005

NOTE A - Summary of Significant Accounting Policies

Authority Formation and Mission

The South County Sewer and Water Authority (the Authority) was established by the Townships of Brady and Pavilion and the Township and Village of Schoolcraft, Kalamazoo County, Michigan. The Authority was incorporated in May, 1997, under the provisions of Act 233, Public Acts of 1955, as amended. The Authority is governed by a board composed of representatives of each of the constituent municipalities. The Authority was formed to operate, maintain, administer and manage a sewage collection and disposal system pursuant to Act 185 Public Acts of 1957, as amended, for the benefit of constituent municipalities.

A nineteen-year bond issue totaling \$6,100,000 financed the cost of the sewer collection system and lines. The bonds were issued in December, 1998. The \$6,100,000 debt will be repaid with proceeds from a twenty-year special assessment roll on benefiting property owners, revenue from new connection fees, and from debt service fees.

Statement on Accounting Policies

The accounting policies of South County Sewer and Water Authority conform to generally accepted accounting principles as applicable to governments. The Authority applies Financial Accounting Standards Board (FASB) pronouncements and Accounting Principle Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict or contradict Governmental Accounting Standards Board (GASB) pronouncements, in which case, GASB prevails. The Authority has elected not to follow FASB pronouncements and APB opinions issued after November 30, 1989.

Effective April 1, 2004, the Authority adopted GASB 34. The most significant change required by the adoption of GASB 34 was the reporting of net assets as shown in the accompanying Statements of Net Assets and the addition of the required supplementary information - Management's Discussion and Analysis. The Authority adopted GASB 40, "Deposits and Investment Risk Activities", for the fiscal years beginning April 1, 2005. GASB 40 affects the nature of the disclosures related to deposits and investment activities of the Authority.

Scope of Reporting Entity and Basis of Presentation

The financial statements of South County Sewer and Water Authority contain all the funds that are financially interdependent on the Authority's executive or legislative branches. The most significant manifestation in determining the reporting entity is financial interdependence. Other manifestations to be considered include, but are not limited to, the selection of governing authority, the designation of management, the ability to significantly influence operations, and accountability for fiscal matters. Another criterion used to evaluate potential component units for inclusion or exclusion in a reporting entity is the existence of special financing relationships regardless of oversight responsibilities. The Authority does not have any potential component units. Based on these criteria, the Authority is considered a reporting unit and is not considered a component unit of the Townships.

SOUTH COUNTY SEWER AND WATER AUTHORITY
NOTES TO FINANCIAL STATEMENTS
For the Years Ended March 31, 2006 and 2005

NOTE A - Summary of Significant Accounting Policies (Continued)

Basis of Accounting

All activities of the Authority are accounted for in a single proprietary fund. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of these funds are included on the statement of net assets. Net assets is divided by the following components: invested in capital assets-net of related debt, restricted for debt service and other purposes, and unrestricted.

Proprietary fund-type operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets. Activities of the Authority are accounted for using the accrual basis of accounting. Revenues are recognized when they are earned and expenses are recognized when they are incurred. Operating activities include all revenues and expenses associated with sewer activities. Non-operating revenues and expenses relate primarily to financing and investing activities.

Use of Restricted Assets

Certain deposits and investments are restricted by contract and/or Township ordinance for debt service purposes, capital improvements, significant repairs and replacements and by Authority policy for future contingencies. Costs of capital improvements and significant repairs and replacements are funded first from restricted assets.

Fixed Assets

Fixed assets of the Authority are accounted for on a cost of services or "capital maintenance" measurement focus. Fixed assets are valued at cost. Donated fixed assets are stated at their fair market value on the date donated.

Depreciation of all exhaustible fixed assets is charged as an expense against operations. Depreciation is calculated using the straight-line method over the estimated useful lives of the related assets as follows: Sewer Lines - 40 years, Sewer Equipment - 7 years, and Office Equipment - 5 years.

Capitalized Interest

Interest costs on debt incurred to finance fixed asset additions is capitalized during the construction period. Interest is capitalized at the rate of the associated debt instrument based on the cost incurred on the related construction until such time as the sewer system is ready for service. The interest capitalized is added to the carrying cost of the sewer system.

SOUTH COUNTY SEWER AND WATER AUTHORITY
NOTES TO FINANCIAL STATEMENTS
For the Years Ended March 31, 2006 and 2005

NOTE A - Summary of Significant Accounting Policies (Continued)

Estimates

Preparation of financial statements in accordance with generally accepted accounting principles requires the use of estimates by management. Estimates are subject to change and, accordingly, actual results may differ from the estimates used in preparation of the accompanying financial statements. These financial statements include estimates primarily as to the depreciable lives and salvage values of fixed assets, and the current portion of contracts receivables.

Cash and Cash Equivalents

For purposes of the statements of cash flows, all highly liquid investments with a maturity of three months or less when purchased that are not restricted for capital additions or debt retirement are considered to be cash equivalents.

Reclassifications

Certain reclassifications were made to the amounts reported in the fiscal 2005 financial statements to conform to classifications used in the fiscal 2006 financial statements.

NOTE B - Cash, Deposits and Investments

The State of Michigan allows a political subdivision to authorize its treasurer or other chief financial officer to invest surplus funds belonging to and under the control of the entity into certain instruments described as follows: bonds and other direct obligations of the United States or an agency of the State of Michigan or its political subdivisions, or instrumentality of the United States; certificates of deposit, savings accounts, deposit accounts, or depository receipts of a bank or savings and loan which is a member of the Federal Deposit Insurance Corporation or a credit union which is insured by the National Credit Union. The Authority may invest in commercial paper rated at the time of purchase within the two highest classifications established by not less than two standard rating services and which matures not more than 270 days after the date of purchase; in United States government or federal obligation repurchase agreements; in bankers' acceptances of United States banks; in mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan and SEC regulated; or in surplus funds investment pools.

Depositories actively used by the Authority during each of the years were: Kalamazoo County State Bank and Investment Centers of America, Inc. The Authority has not established policies to monitor and evaluate custodial credit risk.

Balances at March 31 related to cash and cash equivalents and deposits (including certificates of deposit with greater than 90 day maturities at purchase) are detailed on the statements of net assets as follows:

SOUTH COUNTY SEWER AND WATER AUTHORITY
NOTES TO FINANCIAL STATEMENTS
For the Years Ended March 31, 2006 and 2005

NOTE B - Cash, Deposits and Investments (Continued)

	<u>2006</u>	<u>2005</u>
Cash and cash equivalents	\$ 47,577	\$ 30,181
Restricted assets (See Note D)		
Bank deposits and money market accounts	500,946	469,672
United States government obligations	<u>957,226</u>	<u>1,270,475</u>
TOTALS	<u><u>\$ 1,505,749</u></u>	<u><u>\$ 1,770,328</u></u>

Cash, deposits and United States government obligations (including restricted assets) at March 31, as shown by carrying amount and bank balance and classified by categories of credit risk are itemized as follows:

	<u>2006</u>		<u>2005</u>	
	<u>Carrying Amount</u>	<u>Bank Balance</u>	<u>Carrying Amount</u>	<u>Bank Balance</u>
Cash and deposits				
FDIC insured	\$ 100,000	\$ 100,000	\$ 100,000	\$ 100,000
Uninsured and uncollateralized	190,973	199,251	382,250	388,869
Money Market Mutual Funds				
Insured by SPIC	257,550	257,550	17,603	17,603
United States government obligations				
SPIC insured	242,450	242,450	788,078	774,092
Uninsured	<u>714,776</u>	<u>703,150</u>	<u>482,397</u>	<u>482,397</u>
TOTALS	<u><u>\$ 1,505,749</u></u>	<u><u>\$ 1,502,401</u></u>	<u><u>\$ 1,770,328</u></u>	<u><u>\$ 1,762,961</u></u>

The Authority invests in Federated Capital Reserves (Fund) money market fund. The Fund invests in commercial paper and notes, variable rate instruments, overnight securities, and bank instruments. Approximately 95% of the funds investments credit quality are in the first tier and approximately 5% are in the second tier. The money market investments and a portion of the United States Government Obligations, bonds, are insured by the SPIC, as shown in the schedule above. The SPIC is a private insurer and is not a government insurance agency. The Authority's uninsured cash and deposits are held with Kalamazoo County State Bank.

The Authority's investment in U.S. Government bonds totaled \$957,226 and \$1,270,475 at March 31, 2006 and 2005, respectively. At March 31, 2006, approximately 5% of the bonds matured within 1 month, approximately 33% of the bonds matured within 7 to 12 months, and approximately 62% of the bonds matured between 1 and 5 years after March 31, 2006.

SOUTH COUNTY SEWER AND WATER AUTHORITY
NOTES TO FINANCIAL STATEMENTS
For the Years Ended March 31, 2006 and 2005

NOTE C – Contracts Receivable and Other Contracts Receivable

Contracts receivable from municipalities and Byholt represent balances from special assessment rolls. The rolls will be collected over a twenty-year period, plus interest at 1% over the Authority's cost of funds on the unpaid balance. Individual residents and businesses are legally responsible for payment of the fees. This disperses the credit risk over approximately 450 parcels in the geographic area. The assessments become priority liens on each of the assessed parcels. Additionally, unpaid portions of assessments due become tax liens due and payable in the same manner as property taxes. The amount shown under current assets represents the principal portion of special assessments estimated to be collected in the current year.

Contracts receivable at March 31, consists of the following:

	Current Portion		Total	
	2006	2005	2006	2005
Brady Township	\$ 162,000	\$ 165,000	\$ 1,592,086	\$ 1,790,646
Pavilion Township	33,000	35,000	354,865	404,727
Pavilion Township Special Assessment - Sprinkle	20,000	---	200,000	---
Byholt	7,000	---	94,080	---
Village of Vicksburg	---	---	118,297	---
	<u>\$ 222,000</u>	<u>\$ 200,000</u>	<u>2,359,328</u>	<u>2,195,373</u>
Less current portion			(222,000)	(200,000)
TOTALS			<u>\$ 2,137,328</u>	<u>\$ 1,995,373</u>

Other contracts receivable (connection fees) consist of customers hooking up to the system who are not part of the special assessments. Contract terms vary and include interest, generally at 5.5%. The Authority sets the interest rate annually based on the local interest rate market. Other contracts receivable are secured by property liens on the related parcels. The amount shown under current assets represents the principal portion of other contracts expected to be collected in the current year.

Other contracts receivable at March 31, consists of the following:

	Current Portion		Total	
	2006	2005	2006	2005
Connection fees	<u>\$ 25,000</u>	<u>\$ 20,000</u>	\$ 191,984	\$ 180,447
Less current portion			(25,000)	(20,000)
TOTALS			<u>\$ 166,984</u>	<u>\$ 160,447</u>

SOUTH COUNTY SEWER AND WATER AUTHORITY
NOTES TO FINANCIAL STATEMENTS
For the Years Ended March 31, 2006 and 2005

NOTE D - Restricted Assets

Deposits and investments at March 31, are restricted for the following purposes:

	<u>2006</u>	<u>2005</u>
Reserved for payment on contract debt issued December 1, 1998	\$ 1,375,343	\$ 1,403,675
Reserved for payment on Sprinkle Road debt issued August 8, 2005	2,829	---
Reserved for construction of Sprinkle Road sewer	---	256,472
Reserved for capital improvements	<u>80,000</u>	<u>80,000</u>
TOTAL RESTRICTED DEPOSITS AND INVESTMENTS	<u><u>\$ 1,458,172</u></u>	<u><u>\$ 1,740,147</u></u>

The board determines the reserve for capital improvements annually. Connection fee receipts, to the extent they are not needed for current debt service requirements, are deemed available for capital improvements. The reserve for capital improvements is also provided to cover the Authorities' exposure related to the self-insurance against risk of loss from damage that may be incurred by users of the sewer system from sewer operations/ backups and construction. See Note J.

NOTE E - Property and Equipment

The property and equipment of the Authority, together with changes therein for the year ended March 31, 2006, are detailed as follows:

	<u>Cost</u>			<u>Balances March 31, 2006</u>
	<u>Balances April 1, 2005</u>	<u>Additions</u>	<u>Disposals</u>	
Office equipment	\$ 7,921	\$ 1,231	\$ ---	\$ 9,152
Sewer system	7,268,350	581,604	---	7,849,954
Sewer equipment	<u>2,434</u>	<u>---</u>	<u>---</u>	<u>2,434</u>
Total Property and Equipment	7,278,705	582,835	---	7,861,540

SOUTH COUNTY SEWER AND WATER AUTHORITY
NOTES TO FINANCIAL STATEMENTS
For the Years Ended March 31, 2006 and 2005

NOTE E - Property and Equipment (Continued)

	Accumulated Depreciation			Balances March 31, 2006
	Balances April 1, 2005	Additions	Disposals	
Office equipment	\$ 4,353	\$ 473	---	\$ 4,826
Sewer system	808,752	183,275	---	992,027
Sewer equipment	1,130	348	---	1,478
Total Accumulated Depreciation	814,235	184,096	---	998,331
Net Property and Equipment	<u>\$ 6,464,470</u>	<u>398,739</u>	<u>\$ ---</u>	<u>\$ 6,863,209</u>

NOTE F - Demand Obligation Payable

Certain costs were incurred in connection with the start-up of the Authority. These costs, which are standard and typical for the first several years of operation, were financed with bond proceeds that, under certain circumstances, could revert to the respective townships. Effective August 14, 2000, the Authority, pursuant to township resolution, became contractually obligated to Brady and Pavilion Townships in the aggregate amount of \$150,000. During the year ended 2005, Brady and Pavilion Township forgave the \$150,000 demand obligation and interest accrued to that date of \$26,833. The forgiveness of the debt was recorded as contributed assets.

NOTE G - Changes in Long-term Debt

The following is a summary of debt transactions of the Authority for the years ended March 31, 2006 and 2005:

	Sewer Contract Debt		
	Kalamazoo County	Other	Total
DEBT PAYABLE, MARCH 31, 2004	\$ 5,075,000	\$ 70,520	\$ 5,145,520
Debt retired	<u>(325,000)</u>	<u>---</u>	<u>(325,000)</u>
DEBT PAYABLE, MARCH 31, 2005	4,750,000	70,520	4,820,520
Debt issued	---	428,518	428,518
Debt retired	<u>(350,000)</u>	<u>(77,720)</u>	<u>(427,720)</u>
DEBT PAYABLE, MARCH 31, 2006	<u>\$ 4,400,000</u>	<u>\$ 421,318</u>	<u>\$ 4,821,318</u>

SOUTH COUNTY SEWER AND WATER AUTHORITY
NOTES TO FINANCIAL STATEMENTS
For the Years Ended March 31, 2006 and 2005

NOTE G - Changes in Long-term Debt (Continued)

The contract debt payable at March 31, consists of the following issues:

	<u>2006</u>	<u>2005</u>
\$6,100,000 Kalamazoo County General Obligation Bonds dated December 1, 1998, due in annual principal installments ranging from \$325,000 to \$400,000 through June 1, 2017, plus interest payable semi-annually on June 1 and December 1 of each year at 4.15% to 4.30%.	\$ 4,400,000	\$ 4,750,000
\$215,800 Pavilion Township Installment Purchase Agreement dated August 8, 2005, due in annual installments of principal and interest each April 1 through April 2020, interest rate of 4.8%, secured by Byholt Special Assessment	215,800	---
\$212,718 Pavilion Township Sewer Fund Loan dated September 14, 2005, payable from special assessment and new connections to Sprinkle Road Sewer, interest accrues at Authority's cost of funds (currently 4.3%), interest is payable annually, principal is payable when applicable special assessment or connection fees are collected	205,518	---
\$70,520 Contract payable to City of Portage for excess capacity, interest accrues at 4.4% annually, due in annual installments of \$14,104 plus interest beginning September 1, 2005.	---	70,520
	<u>4,821,318</u>	<u>4,820,520</u>
Less current maturities	<u>(371,000)</u>	<u>(350,000)</u>
TOTALS	<u>\$ 4,450,318</u>	<u>\$ 4,470,520</u>

SOUTH COUNTY SEWER AND WATER AUTHORITY
NOTES TO FINANCIAL STATEMENTS
For the Years Ended March 31, 2006 and 2005

NOTE G - Changes in Long-term Debt (Continued)

The minimum annual debt service requirements, including interest, for long-term debt outstanding as of March 31, 2006 are as follows:

Years Ending March 31,	Principal	Interest	Totals
2007	\$ 371,000	\$ 200,392	\$ 571,392
2008	371,000	184,212	555,212
2009	371,000	168,254	539,254
2010	371,000	152,558	523,558
2011	406,800	136,950	543,750
2012-2016	2,128,000	406,850	2,534,850
2017-2021	802,518	36,356	838,874
TOTALS	\$ 4,821,318	\$ 1,285,572	\$ 6,106,890

The Pavilion Township Sewer Fund debt of \$205,518 is payable from a special assessment and new connections to the Sprinkle Road extension. The expected future maturities of this debt have been reported based on the expected repayments of the related special assessment without considering future connections.

For the years ended March 31, 2006 and 2005, the Authority paid interest costs of \$219,037 and \$211,023, respectively. The Authority did not capitalize any interest charges during the years ended March 31, 2006 and 2005.

NOTE H - Retirement Plan

The Authority maintains a Simple IRA Plan, which allows employees to contribute up to \$6,000 per year to the plan. The Authority is required to make a contribution to the plan annually, as defined in the plan document. Contributions to the plan totaled \$1,329 and \$1,310 for the years ended March 31, 2006 and 2005, respectively.

NOTE I - Non-cash Activities

For the year ended March 31, the Authority had the following non-cash activity:

	2006	2005
Assessment rolls added	<u>\$ 415,800</u>	<u>\$ ---</u>
Connection fee contracts added	<u>\$ 82,000</u>	<u>\$ 62,410</u>
Demand obligation payable plus accrued interest payable contributed to Authority	<u>\$ ---</u>	<u>\$ 176,835</u>

SOUTH COUNTY SEWER AND WATER AUTHORITY
NOTES TO FINANCIAL STATEMENTS
For the Years Ended March 31, 2006 and 2005

NOTE J – Insurable Risk

The Authority, in the normal operation of its activities, has exposure for damage to residential and commercial property and personal injury resulting from the operation or construction of its sewer system. The Authority Board has elected to self-insure against this risk. The Authority Board believes that funds accumulated and restricted for significant replacements, as disclosed in Note D, are adequate to cover the associated risk.

SUPPLEMENTAL INFORMATION

SOUTH COUNTY SEWER AND WATER AUTHORITY
SCHEDULE OF OPERATING EXPENSES COMPARED TO BUDGET
For the Year Ended March 31, 2006
(Comparative Actual Amounts for the Year Ended March 31, 2006)

	2006		Variance –	2005
	Budget	Actual	Favorable (Unfavorable)	Actual
Salaries and wages	\$ 51,750	\$ 50,605	\$ 1,145	\$ 49,166
Fringe benefits:				
Social security	4,160	3,975	185	3,758
Insurance	4,925	4,740	185	4,790
Retirement	1,329	1,329	---	1,311
	<u>10,414</u>	<u>10,044</u>	<u>370</u>	<u>9,859</u>
Contracted services:				
Insurance/workman's compensation	7,000	6,442	558	6,301
Contracted services	23,200	24,965	(1,765)	25,120
Treatment charges	45,900	51,149	(5,249)	38,225
Engineering	1,500	704	796	470
Publications/ printing	112	90	22	84
Audit	3,900	3,900	---	3,700
Legal	1,500	367	1,133	506
Mileage/travel/entertainment	750	380	370	336
Miss Dig fees	400	379	21	371
Rent	2,400	2,400	---	2,400
Bank fees	100	47	53	42
Alarm system	400	410	(10)	---
Education and subscriptions	300	99	201	---
	<u>87,462</u>	<u>91,332</u>	<u>(3,870)</u>	<u>77,555</u>
Utilities:				
Electric and gas	10,500	8,378	2,122	10,297
Telephone	1,500	1,441	59	1,257
	<u>12,000</u>	<u>9,819</u>	<u>2,181</u>	<u>11,554</u>
Supplies:				
Postage	1,300	1,296	4	1,141
Office	2,000	2,436	(436)	2,060
	<u>3,300</u>	<u>3,732</u>	<u>(432)</u>	<u>3,201</u>
Maintenance and repairs:				
General maintenance	1,000	3,312	(2,312)	916
Repairs and maintenance reimbursement	3,000	3,761	(761)	3,610
	<u>4,000</u>	<u>7,073</u>	<u>(3,073)</u>	<u>4,526</u>
Miscellaneous	328	---	328	---
TOTALS, EXCLUDING DEPRECIATION	<u>\$ 169,254</u>	<u>\$ 172,605</u>	<u>\$ (3,351)</u>	<u>\$ 155,861</u>

See Accompanying Independent Auditors' Report

**SOUTH COUNTY SEWER AND WATER AUTHORITY
SCHEDULE OF PRINCIPAL AND INTEREST PAYMENTS
\$6,100,000 KALAMAZOO COUNTY GENERAL OBLIGATION BONDS
DATED DECEMBER 1, 1998
For the Year Ended March 31, 2006**

Years Ending March 31,	Rate	Principal June 1	Interest		Totals
			June 1	December 1	
2007	4.30	\$ 350,000	\$ 94,250	\$ 86,725	\$ 530,975
2008	4.30	350,000	86,725	79,200	515,925
2009	4.30	350,000	79,200	71,675	500,875
2010	4.15	350,000	71,675	64,412	486,087
2011	4.25	350,000	64,412	56,975	471,387
2012	4.30	375,000	56,975	48,913	480,888
2013	4.30	375,000	48,912	40,850	464,762
2014	4.30	375,000	40,850	32,788	448,638
2015	4.30	375,000	32,788	24,725	432,513
2016	4.30	375,000	24,725	16,662	416,387
2017	4.30	375,000	16,663	8,600	400,263
2018	4.30	400,000	8,600	---	408,600
TOTALS		<u>\$ 4,400,000</u>	<u>\$ 625,775</u>	<u>\$ 531,525</u>	<u>\$ 5,557,300</u>

See Accompanying Independent Auditors' Report

**SOUTH COUNTY SEWER AND WATER AUTHORITY
SCHEDULE OF PRINCIPAL AND INTEREST PAYMENTS
PAVILION TOWNSHIP INSTALLMENT PURCHASE AGREEMENT
DATED AUGUST 8, 2005
For the Year Ended March 31, 2006**

<u>Years Ending March 31,</u>	<u>Rate</u>	<u>Principal March 31</u>	<u>Interest March 31</u>	<u>Totals</u>
2007	4.80	\$ 1,000	\$ 10,358	\$ 11,358
2008	4.80	1,000	10,310	11,310
2009	4.80	1,000	10,262	11,262
2010	4.80	1,000	10,214	11,214
2011	4.80	36,800	10,166	46,966
2012	4.80	36,000	8,400	44,400
2013	4.80	36,000	6,672	42,672
2014	4.80	37,000	4,944	41,944
2015	4.80	37,000	3,168	40,168
2016	4.80	7,000	1,392	8,392
2017	4.80	7,000	1,056	8,056
2018	4.80	7,000	720	7,720
2019	4.80	6,000	384	6,384
2020	4.80	2,000	96	2,096
TOTALS		<u>\$ 215,800</u>	<u>\$ 78,142</u>	<u>\$ 293,942</u>

See Accompanying Independent Auditors' Report

**SOUTH COUNTY SEWER AND WATER AUTHORITY
SCHEDULE OF PRINCIPAL AND INTEREST PAYMENTS
PAVILION TOWNSHIP SEWER FUND LOAN
DATED SEPTEMBER 14, 2005
For the Year Ended March 31, 2006**

<u>Years Ending March 31,</u>	<u>Rate</u>	<u>Principal* March 31</u>	<u>Interest March 31</u>	<u>Totals</u>
2007	4.30	\$ 20,000	\$ 9,059	\$ 29,059
2008	4.30	20,000	7,977	27,977
2009	4.30	20,000	7,117	27,117
2010	4.30	20,000	6,257	26,257
2011	4.30	20,000	5,397	25,397
2012	4.30	20,000	4,537	24,537
2013	4.30	20,000	3,677	23,677
2014	4.30	20,000	2,817	22,817
2015	4.30	20,000	1,957	21,957
2016	4.30	20,000	1,097	21,097
2017	4.30	<u>5,518</u>	<u>237</u>	<u>5,755</u>
TOTALS		<u>\$ 205,518</u>	<u>\$ 50,129</u>	<u>\$ 255,647</u>

* Interest is payable annually. Principal is repayable as payments are made on a special assessment to the Sprinkle Road Sewer and as new connections (not part of the special assessment district) are made to the Sprinkle Road Sewer Extension. The above payment schedule is based on the contractual receipts of the Sprinkle Road Special Assessment District without considering new connect fees.

SEBER TANS, PLC

CONSULTANTS & CERTIFIED PUBLIC ACCOUNTANTS

To the Board of Commissioners and
Director of South County Sewer and
Water Authority

In planning and performing the audit of the financial statements of South County Sewer & Water Authority for the year ended March 31, 2006, we considered the Authority's internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control structure. However, we noted certain matters involving internal control and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control system that, in our judgment, could adversely affect South County Sewer & Water Authority's ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial statements.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that errors or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of internal control would not necessarily disclose all matters in internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we noted the following reportable conditions that we believe to be material weaknesses.

Separation of duties

Due to the small size of the Authority's office staff (two personnel), separation of duties is limited. The office manager has access to assets, recording of the assets and reconciliation functions. The general manager initiates and authorizes all significant transactions. As a result, the risk of loss, error, or irregularities of assets increases. We recommend that the Authority Supervisors review key financial reports and reconciliations periodically for unusual matters. In addition, fidelity bonds as discussed below should adequately cover all personnel with access to accounting records and assets of the Authority.

Employee bonding

The Authority has bonded its employees and Board members for \$100,000. The Authority has cash and highly liquid assets well in excess of \$1,000,000. We recommend that the Authority increase its bond coverage.

We also noted the following reportable conditions that are not believed to be material weaknesses.


Collateralizing bank balances in excess of \$100,000

The Authority maintains several cash accounts with a bank. The balances exceed the FDIC insurance limit of \$100,000. Should the bank fail, the Authority may incur a loss if the cash invested at the bank exceeds the insurance limits. We recommend that the Authority monitor the financial condition of the bank and that it continue its efforts to obtain collateral for balances in excess of FDIC insurance limits. The Authority may request banks to pledge securities for payment of any uninsured losses or it may consider investing in other insured financial instruments.

Evaluation of debt repayment

The assessment receivable balance is considerably less than the bond payable balance. Additionally, interest rates on investments are at a historically low rate. These conditions may result in early payoffs of assessments receivable and add to the difficulty of repaying the bonds. We recommend that the Authority continue their annual evaluation of the bond repayment schedule and take all necessary steps to provide for the payment of its long-term debt, including increasing debt service payments.

This report is intended solely for the information and use of the Board of Commissioners and Management of South County Sewer & Water Authority, and is not intended to be and should not be used by anyone other than these specified parties.


Seber Tans, PLC
July 14, 2006

SEBER TANS, PLC

CONSULTANTS & CERTIFIED PUBLIC ACCOUNTANTS

July 14, 2006

To the Board of Commissioners and Director
South County Sewer & Water Authority

We have audited the financial statements of South County Sewer & Water Authority (the Authority) for the year ended March 31, 2006, and have issued our report thereon dated July 14, 2006. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility under Auditing Standards Generally Accepted in the United States of America and Government Auditing Standards

As stated in our engagement letter dated February 16, 2006, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance about whether the financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because an audit is designed to provide reasonable, but not absolute, assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

In planning and performing our audit, we considered the Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting.

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit.

Significant Accounting Policies

Management has the responsibility for selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the Authority are described in Note A to the financial statements. The Authority implemented GASB 40, deposit and investment risk disclosures, in fiscal 2006. The Authority did not adopt any other new accounting policies nor did they change the application of existing policies during the year. We noted no transactions entered into by the Authority during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements was depreciation and debt service projections.

We evaluated the key factors and assumptions used for depreciation and debt service requirements in determining that they are reasonable in relation to the financial statements taken as a whole.

Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the Authority's financial reporting process (that is, cause future financial statements to be materially misstated). We proposed, and management recorded, numerous adjustments caused by mispostings and accruals not made by the Authority.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the Authority's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principals and auditing standards, with management each year prior to retention as the Authority's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing our audit.

This information is intended solely for the use of the Board of Directors, the Finance/Audit Committee, and management of the Authority and is not intended to be and should not be used by anyone other than these specified parties.

Very Truly Yours,

Seber Tans, PLC
Seber Tans, PLC